

shareholders and to the Funding Corporation for disclosure to investors;

(iii) Oversee the audit activities of the external auditor; and

(iv) Monitor internal controls, including those relating to compliance with laws and regulations.

Subpart B—Annual Report to Investors

§ 630.20 Contents of the annual report to investors.

The annual report shall contain the following:

(a) *Description of business.* (1) The description shall include a brief discussion of the following:

(i) The System's overall organizational structure, its lending institutions by type and their respective authorities, the relationships between different types of institutions, and the overall geographic area and eligible borrowers served by those institutions;

(ii) The types of lending activities engaged in and financial services offered by System institutions;

(iii) Any significant developments within the last 5 years that have had or could have a material impact on the System's organizational structure and the manner in which System institutions conduct business, including, but not limited to, statutory or regulatory changes, mergers or liquidations of System institutions, terminations of System institution status, and financial assistance provided by or to System institutions through loss-sharing or capital preservation agreements or from any other source;

(iv) Any acquisition or disposition of material assets during the last fiscal year that took place outside the ordinary course of business;

(v) Any concentrations of more than 10 percent of total assets in particular types of agricultural activities or businesses, and any dependence of an institution or a group of institutions of the System upon a specific activity or business, a single customer, or a few customers, including other financing institutions (OFIs), the loss of any one of which would have a material effect on the System; and

(vi) The authority of System institutions to purchase and sell interests in

loans in secondary markets and the risk involved in such activities.

(2) List the address of the headquarters of each disclosure entity and service organization of the System.

(b) *Federal regulation and insurance—*
(1) *Farm Credit Administration.* Describe the regulatory and enforcement authority of the FCA over System institutions under the Act.

(2) *Farm Credit System Insurance Corporation.* (i) Describe the role and authorities of the Farm Credit System Insurance Corporation (FCSIC) under part E of title V of the Act. Describe specifically the role of the FCSIC in insuring the timely payment of principal and interest on FCS debt obligations and in providing assistance to System institutions.

(ii) Describe the FCSIC's status as a Government corporation and state that System institutions have no control over the management of the FCSIC or the discretionary expenditures from the Farm Credit Insurance Fund (Insurance Fund), which are the sole prerogative of the FCSIC.

(3) *Farm Credit System Financial Assistance Corporation.* Describe the role and authorities of the Financial Assistance Corporation under title VI of the Act, debt obligations of the Financial Assistance Corporation issued to provide financial assistance to the System, and statutory repayment obligations of System institutions.

(c) *Description of legal proceedings and enforcement actions.* (1) Describe any material pending legal proceedings in which one or more System institutions are a party, or that involve claims that a System institution(s) may be required by contract or operation of law to satisfy, and the potential impact of such proceedings, to the extent known, on the System.

(2) Provide a summary of the types of enforcement actions in effect during the year, and any material impact of such proceedings on the System.

(d) *Description of liabilities.* (1) Describe how the System funds its lending operations, including:

(i) System banks' authority to borrow, and issue notes, bonds, debentures, and other obligations, and limitations thereof under section 4.2 of the Act;

(ii) A description of the types of debt obligations authorized to be issued under the Act, the types of debt obligations currently issued, the manner and form in which they are issued, rights of securities holders, risk factors, use of proceeds, tax effects of holding securities, market information, and other pertinent information;

(iii) For each of the types of obligations that may be issued, whether it is insured, and the extent of any joint and several liability for the obligations; and

(iv) Any applicable statutory and regulatory requirements affecting a bank's ability to incur debt.

(2) Describe agreements among System banks and the Funding Corporation affecting a bank's ability to incur debt.

(3) Describe agreements among System institutions regarding capital preservation, loss sharing, or any other forms of financial assistance.

(e) *Description of capital.* (1) Describe the capitalization of the System, including capital structure, types of stock and participation certificates, and voting rights of holders of stock and participation certificates.

(2) Describe the statutory requirement that a borrower purchase stock as a condition of obtaining a loan; how such stock is purchased, transferred, and retired; and how earnings are distributed.

(3) Describe any statutory or other authority of a System institution to require additional capital contributions from stockholders.

(4) Describe regulatory minimum permanent capital standards and capital adequacy requirements for banks and associations. State the number of institutions, if any, categorized by banks and associations, that are not currently in compliance with such standards and include a brief discussion of the reasons for the noncompliance.

(5) Describe any statutory and regulatory restrictions on retirement of stock and distribution of earnings by System institutions. State the number of System institutions, if any, categorized by banks and associations, that are currently affected by such re-

strictions and provide a summary of the causes of such prohibitions.

(f) *Selected financial data.* At a minimum, furnish the following combined financial data of the System in comparative columnar form for each of the last 5 fiscal years.

(1) *Balance sheet.*

(i) Loans.

(ii) Allowance for losses.

(iii) Net loans.

(iv) Cash and investments.

(v) Other property owned.

(vi) Total assets.

(vii) FCS debt obligations and other bonds, notes, debentures, and obligations, presented by type, with a descriptive title.

(viii) Total liabilities.

(ix) Capital stock and surplus.

(2) *Statement of income.*

(i) Net interest income.

(ii) Net other expenses.

(iii) Provision for loan losses.

(iv) Extraordinary items.

(v) Provision for income taxes.

(vi) Net income (loss).

(3) *Key financial ratios.* (i) Return on average assets.

(ii) Return on average capital stock and surplus.

(iii) Net interest income as a percentage of average earning assets.

(iv) Net loan chargeoffs as a percentage of average loans.

(v) Allowance for loan losses as a percentage of gross loans outstanding at yearend.

(vi) Capital stock and surplus as a percentage of total assets at yearend.

(vii) Debt to capital stock and surplus at yearend.

(g) *Discussion and analysis.* Fully discuss any material aspects of financial condition, changes in financial condition, and results of operations of System institutions, on a combined basis, for the comparative years required by paragraph (g)(6)(ii) of this section or such other time periods specified in the following paragraphs of this section. Identify favorable and unfavorable trends, and significant events or uncertainties necessary to understand the financial condition and results of operations of the System. At a minimum, the discussion shall include the following:

(1) *Loan portfolio*—(i) *Categorization*. Describe the loan portfolio of the System by major loan purpose category, indicating the amount and approximate percentage of the total dollar portfolio represented by each major category.

(ii) *Risk exposure*. (A) Describe and analyze all high-risk assets, including an analysis of the nature and extent of significant current and potential credit risks within the loan portfolio and of other information that could adversely affect the loan portfolio and other property owned.

(B) Provide an analysis of the allowance for loan losses that includes the ratios of the allowance for loan losses to loans (outstanding at yearend) and net chargeoffs to average loans, and a discussion of the adequacy of the allowance for loan losses to absorb the risk inherent in the loan portfolio and the basis for such determination.

(iii) *Secondary market activities*. (A) If material, quantify System institutions' secondary market activities and the risk involved in such activities.

(B) If material, provide an analysis of historical loss experience and the amount provided for risk of loss associated with secondary market activities.

(2) *Results of operations*. (i) Describe, on a comparative basis, changes in the major components of net interest income. Include a discussion of significant factors that contributed to the changes and quantify the amount of change(s) due to an increase or decrease in volume and the amount due to changes in interest rates earned and paid, based on averages for each period.

(ii) Describe any unusual or infrequent events or transactions, or any significant economic changes that materially affected reported income and, in each case, indicate the extent to which income was so affected.

(iii) Discuss the factors underlying any material changes in the return on average assets and return on average capital stock and surplus.

(iv) Describe, on a comparative basis, the major components of operating expense and any other significant components of income or expense, indicating the reasons for any significant increases or decreases.

(v) Describe any known trends or uncertainties that have had, or that are reasonably expected to have, a material impact on net interest income or net income. Disclose any known events that will cause a material change in the relationship between costs and revenues.

(vi) Explain the changes that have taken place, by major components on a comparative basis, in Insurance Fund assets and related restricted capital and how such changes affected reported income.

(3) *Funding sources and liquidity*—(i) *Funding sources*. (A) Provide, in tabular form, the component amounts and the total amount of FCS debt obligations, debt obligations issued by banks individually, and Financial Assistance Corporation debt obligations outstanding at yearend for each of the past 2 fiscal years. List debt obligations issued by System institutions separately by type, also separating insured obligations from uninsured obligations. For each type of debt obligation listed, provide the following, at a minimum, for each fiscal year listed:

(1) The beginning balance, the total amount of debt issued, the total amount of debt retired, and the yearend balance; and

(2) The average maturities and average interest rates on debt outstanding at yearend, and the average maturities and average interest rates of new debt issued during the year.

(B) Summarize any other sources of funds, including lines of credit with commercial lenders, and their terms.

(ii) *Liquidity*. (A) Include a brief overview of any FCA regulations or System policies with regard to liquidity and liquidity reserves.

(B) Identify any known trends, demands, commitments, events, or uncertainties that will result in, or that are reasonably likely to result in, System liquidity increasing or decreasing in any material way. If a material liquidity deficiency is identified, indicate the course of action that has been taken or is proposed to be taken by management of affected System institutions to remedy the deficiency.

(iii) *Investment*. Provide a brief overview of the System's investment policies and objectives, any regulatory

limitations thereon, and the contents of the System's existing investment portfolio.

(iv) *Interest rate sensitivity.* (A) Provide a brief overview of the System's asset and liability management practices, including interest rate risk measurement systems, and methods used to control interest rate risk, such as the use of investments, derivatives, and other off-balance-sheet transactions.

(B) Provide an analysis of the System's exposure to interest rate risk and its ability to control such risk.

(4) *Capital resources.* (i) Describe any material commitments to purchase capital assets and the anticipated sources of funding.

(ii) Describe any material trends, favorable or unfavorable, in the System's capital resources, including any material changes in the mix of capital and debt, the relative cost of capital resources, and any off-balance-sheet financing arrangements.

(iii) Provide a general discussion of any trends, commitments, contingencies, or events that are reasonably likely to have a material adverse effect on System institutions' ability to comply with regulatory capital standards.

(5) *Insurance Fund.* (i) Describe the purposes for which expenditures from the Insurance Fund may be made and the statutory requirements for making such expenditures.

(ii) Provide a schedule itemizing the amount of Insurance Fund assets that have been specifically identified by the FCSIC for payment of estimated obligations of the FCSIC and the amount of Insurance Fund assets for which no specific use has been identified or designated by the FCSIC. Information provided shall be as of the end of the most recent fiscal year.

(iii) Explain how FCSIC expenditures or designations of Insurance Fund assets for payment of future obligations affect the combined assets and capital of the System, and quantify the effect, if any.

(6) *Instructions for discussion and analysis.* (i) The purpose of the discussion and analysis (D&A) shall be to provide to investors and other users information relevant to an assessment of the combined financial condition and re-

sults of operations of System institutions as determined by evaluating the amounts and certainty of cashflows from operations and from outside sources. The information provided pursuant to this section need only include that which is available to System institutions and which does not clearly appear in the combined financial statements.

(ii) The D&A of the financial statements and other statistical data shall be presented in a manner designed to enhance a reader's understanding of the combined financial condition, results of operations, cashflows, and changes in capital of System institutions. Unless otherwise specified in § 630.20(g), the discussion shall cover the period covered by the financial statements and shall use year-to-year comparisons or any other understandable format. Where trend information is relevant, reference to the 5-year selected financial data required by paragraph (f) of this section may be necessary.

(iii) The D&A shall focus specifically on material events and uncertainties known at the time of reporting that would cause reported financial information not to be necessarily indicative of future operating results or of future financial condition. This should include descriptions and amounts of:

(A) Matters that would have an impact on future operations but that have not had an impact in the past; and

(B) Matters that have had an impact on reported operations but are not expected to have an impact on future operations.

(h) *Directors and management—(1) Board of directors.* Briefly describe the composition of boards of directors of the disclosure entities. List the name of each director of such entities, including the director's term of office and principal occupation during the past 5 years, or state that such information is available upon request pursuant to § 630.3(f).

(2) *Management.* List the names of chief executive officers and presidents of disclosure entities, including position title, length of service at current position, and positions held during the past 5 years.

(i) *Compensation of directors and senior officers.* State that information on the compensation of directors and senior officers of System banks is contained in each bank's annual report to shareholders and that the annual report of each bank is available to investors upon request pursuant to § 630.3(f).

(j) *Related party transactions.* (1) Briefly describe how System institutions, in the ordinary course of business and subject to regulation by the FCA, may enter into loan transactions with related parties, including their directors, officers, and employees, the immediate family members (as defined in § 620.1(e) of this chapter) of such persons, and any organizations with which such persons and their immediate family members are affiliated.

(2) On a comparative basis for each of the fiscal years covered by the balance sheet, state the aggregate amount of the following:

- (i) Loans made to related parties;
- (ii) Loans outstanding at yearend to related parties;
- (iii) Loans outstanding at yearend to related parties that are made on more favorable terms than those prevailing at the time for comparable transactions with unrelated borrowers; and
- (iv) Loans outstanding at yearend to related parties that involve more than a normal risk of collectibility (as defined in § 620.1(i) of this chapter).

(k) *Relationship with independent public accountant.* If a change in the accountant who has previously examined and expressed an opinion on the Systemwide combined financial statements has taken place since the last annual report to investors or if a disagreement with an accountant has occurred that the Funding Corporation would be required to report to the FCA under part 621 of this chapter, disclose the information required by § 621.4(c) and (d) of this chapter.

(l) *Financial statements.* Furnish Systemwide combined financial statements and related footnotes prepared in accordance with GAAP, and accompanied by supplemental information prepared in accordance with the requirements of § 630.20(m). The Systemwide combined financial statements shall provide investors and potential investors in FCS debt obligations with

the most meaningful presentation pertaining to the financial condition and results of operations of the System. The Systemwide combined financial statement and accompanying supplemental information shall be audited in accordance with generally accepted auditing standards by a qualified public accountant (as defined in § 621.2(i) of this chapter). The Systemwide combined financial statements shall include the following:

(1) A balance sheet as of the end of each of the 2 most recent fiscal years; and

(2) Statements of income, statements of changes in capital stock and surplus (or, if applicable, statements of changes in protected borrower capital and capital stock and surplus), and statements of cash flows for each of the 3 most recent fiscal years.

(m) *Supplemental information.* Furnish supplemental information regarding the components of the Systemwide combined financial statements that has been prepared in accordance with the requirements of this paragraph and any additional guidance or instructions provided by the FCA.

(1) At a minimum, the supplemental information shall include the following:

(i) Supplemental balance sheet information as of the end of the most recent fiscal year; and

(ii) Supplemental income statement information for the most recently completed fiscal year.

(2) At a minimum, the report shall present supplemental information showing combined financial data for the following components on a stand-alone basis:

- (i) Banks;
- (ii) Associations;
- (iii) Financial Assistance Corporation;
- (iv) Combined financial data of the System without the Insurance Fund;
- (v) The Insurance Fund and related combination entries; and
- (vi) Combined financial data of the System with the Insurance Fund.

(3) The supplemental information shall be presented in a columnar format and include, at a minimum, the selected financial data listed in the schedules in appendix A of this part.

The prescribed components shall be designated as column headings and they may be abbreviated in the schedules. The financial data required by § 630.20(m)(2)(i) shall include the financial data required to be submitted by each bank pursuant to the requirement of § 630.4(c)(1)(i).

(4) The supplemental information may be presented separately or in accompanying notes to the Systemwide combined financial statements and shall contain additional disclosures sufficient to explain the basis of the presentation of the supplemental information, the components, and any adjustments contained therein to enable readers to understand the effect of each component on the Systemwide combined financial statements.

(n) List the names of the System Audit Committee members in the report to investors.

(o) Include a detailed index setting forth the major disclosure captions of this subpart and the page or pages on which the required information appears in the report.

[59 FR 46742, Sept. 12, 1994, as amended at 63 FR 36549, July 7, 1998]

Subpart C—Quarterly Reports to Investors

§ 630.40 Contents of the quarterly report to investors.

(a) *General.* The quarterly report to investors shall contain the information specified in this section along with any other material information necessary to make the required disclosures, in light of the circumstances under which they are made, not misleading. The quarterly report must be presented in a format that is easily understandable and not misleading.

(b) *Rules for condensation.* For purposes of this subpart, major captions to be provided in interim financial statements are the same as those provided in the financial statements contained in the annual report to investors, except that the financial statements included in the quarterly report may be condensed into major captions in accordance with the rules prescribed under this paragraph.

(1) *Interim balance sheets.* When any major balance sheet caption is less

than 10 percent of total assets and the amount in the caption has not increased or decreased by more than 25 percent since the end of the preceding fiscal year, the caption may be combined with others.

(2) *Interim statements of income.* When any major income statement caption is less than 15 percent of average net income for the 3 most recent fiscal years and the amount in the caption has not increased or decreased by more than 20 percent since the corresponding interim period of the preceding fiscal year, the caption may be combined with others. In calculating average net income, loss years should be excluded. If losses were incurred in each of the 3 most recent fiscal years, the average loss shall be used for purposes of this test.

(3) The interim financial information shall include disclosure either on the face of the financial statements or in accompanying footnotes sufficient to make the interim information presented not misleading. It may be presumed that users of the interim financial information have read or have access to the audited financial statements for the preceding fiscal year, and the adequacy of additional disclosure needed for a fair presentation may be determined in that context. Accordingly, footnote disclosure that would substantially duplicate the disclosure contained in the most recent audited financial statements (such as a statement of significant accounting policies and practices) and details of accounts that have not changed significantly in amount or composition since the end of the most recently completed fiscal year may be omitted.

(4) Interim reports shall disclose events that have occurred subsequent to the end of the most recently completed fiscal year that have a material impact on the System. Disclosures should encompass, for example, significant changes since the end of the most recently completed fiscal year in such items as accounting principles and practices, estimates used in the preparation of financial statements, status of long-term contracts, capitalization, significant new indebtedness or modification of existing financing agreements, financial assistance received,